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A few decades ago, China was amongst the poorest countries in the world. Today, it is enjoying unprecedented growth and is poised to become one of the strongest engines of economic growth globally.

In fact, China's remarkable progress is often cited as an important driving force in reducing poverty in this country of over 1.3 billion people. According to official statistics, there were 260 million people living in poverty in 1978. This figure dropped drastically over the next two decades to 42 million in 1998, and to 28 million by 2002. Is this a success story of the market triumphing over the state? After all, the positive impacts of the agricultural reforms and market liberalisation that took place in the post-Mao era (from 1978 onwards) seem to support those who advocate market reforms to fuel economic growth and reduce poverty, without the need for state interventions.

Singapore Management University political science professor John Donaldson, in his paper "The State, the Market, Economic Growth and Poverty in China", argues that economic growth alone does not necessarily lead to a reduction in poverty. More importantly, even as China underwent market reforms and emerged with impressive results, the role of the state did not actually diminish. On the contrary, points out Donaldson, "the role of the state has instead shifted to other vital roles, establishing new institutions and adopting new functions that both facilitate and alter market forces." According to him, in order to understand poverty reduction in China or anywhere, the relationship between the market and the state should not be seen as a "zero-sum" game but should be combined "in an analytically meaningful way that helps us understand their roles in poverty reduction". To do this, Donaldson focuses on an important aspect of China's reform era between 1978 and 1984 – the de-communisation and reform of agriculture.

Agricultural Reform

In response to political pressure from farmers and local governments, the state gradually replaced the old communal system that had been in place since the mid-1950s, by dividing the land equally amongst people in rural areas and signing long-term leases with them. Although these rural households did not have ownership rights over the land, decision-making on agriculture production was decentralised through the new household responsibility system. Each household was no longer obligated to produce grains first, and were given more freedom to decide what and how much to grow. According to Donaldson's paper, between 1978 and 1984, agricultural production increased on average by 6.6% annually. In fact, growth in the agriculture sector exceeded that of the industrial sector and, for the first time, narrowed the "the urban-rural rich-poor gap" as rural poverty declined rapidly in many areas.

According to Donaldson, advocates of market-led development argued that, as the state decentralised agricultural production through the household responsibility system, it "allowed market forces to determine prices, increasing incentives for productivity in agriculture and spurring economic growth". In addition, they believed that rapid economic growth had directly benefited the rural poor. On the surface, it appears that they could be correct, but Donaldson peels away the layers to show that the situation isn't that simple. He comments, "the actual story of what reduced poverty between 1978 and1984 and beyond is much more complex".

Commodity Quotas

A critical factor in poverty reduction during this period was the establishment of quotas. Under the household responsibility system, each family was to produce certain government-established quotas which the state then purchased at set prices. These prices rose over the first few years. Even though the state would purchase grain produced above the quota, farmers were also allowed to sell such above-quota production in the local markets.

During this period, state purchases of grain proved to be critical in encouraging production and reducing poverty. Quotas allowed the government to alter purchase prices to spur production. For example, during the initial years, according to the paper, the government paid 50% over quota prices for grain. Says Donaldson, "When this policy was rescinded a few years later, the rate of poverty reduction flattened out".

In effect, the role of the state in poverty reduction was greater than what some scholars had argued. As reforms took place, the state was able to mitigate the risks farmers were exposed to. "It was compelled by policy to purchase all the grain that farmers offered at the above-quota price," says Donaldons. Also, guaranteed purchases by the state meant that farmers could sell to a single buyer without having to look for other buyers on the open market. Another advantage, states the paper, was that "quotas provided a buffer against falling market prices, creating a price floor for many commodities". This proved crucial in the early 1980s when production peaked.

The role which the state played in reducing poverty is further supported by other evidence. For example, government procurement significantly influenced rates of grain production and poverty reduction. Between the mid-1980s to early 1990s, when quota price was slashed, grain production and the rate of poverty reduction fell correspondingly. When the state raised quota price by 40% in 1994 and 42% in 1995, agricultural production and poverty reduction increased. More interestingly, despite being able to sell in the open market, farmers continued to sell their grains produced above quota to the state. According to the paper, during the period 1978 to 1984, when poverty levels dropped and production grew , no more than 10% of total grain production was sold on the open market. In contrast, during 1985 to 1987, when grain production fell and poverty levels increased, the proportion of grain production sold on the free market rose to between 16 to 21%.

Land Distribution

Another critical factor in poverty reduction during this period says the paper, was "free and equal distribution of land to rural households based on family size". Though farmers did not have ownership rights ("land usage rights could not be bought and sold and, if abandoned, would be returned to the state for reallocation"), the long-term leases proved an excellent incentive. "They encouraged farmers to improve and irrigate land, and to increase productivity. In this way, the land became a form of insurance," says Donaldson. It allowed farmers to attempt "productive but risky endeavors, such as migrating to cities for work, with the land in typical years providing at least a subsistence income to fall back on".

At this juncture, it might be interesting to examine the relationship between economic growth and poverty reduction. During this period, while rural poverty declined rapidly, economic growth was slowing down. In parallel to the rate of GDP growth, which rose and peaked in 1984 and 1985, poverty rates actually increased and the gap between the rich and the poor widened. However, as the poverty reduction rate picked up momentum in the early 1990s, the rate of increase for per capita GDP slowed. Explains Donaldson, "time lags between the effects on economic growth and poverty cannot explain at least the first two periods, since the poverty reduction was not preceded by rapid economic growth".

Thus economic growth and poverty reduction are not always associated and, as Donaldson argues, economic growth does not necessarily benefit the poor and bring about poverty reduction. According to a World Bank report, throughout the 1990s, the "income of China's richest 1% grew four times as fast as that of other groups". Nevertheless, this does not mean that economic growth has no positive impacts on poverty reduction. Says Donaldson, "understanding the linkage between economic growth and poverty reduction in China and elsewhere requires disaggregating the periods and tracing the actual causal connections , if any, that linked the growth with poverty reduction".

World Bank researchers Ravallion and Chen started this process and identified economic growth in the agricultural sector as a major contributor in improving the incomes of the poor. So significant was the contribution of agricultural production to rural poverty reduction during this period that the impact of economic growth in the agricultural sector on livelihoods was four times the growth in the industrial or service sectors.

The paper concludes that none of this would have been possible without the involvement of the state. Firstly, in implementing the household responsibility system, a strong state is needed to ensure as fair a redistribution of land as possible, which was based on household size and not "local power". The active involvement of the state to establish appropriate institutions and enforce laws is essential for ensuring the success of land reform. Secondly, the state influenced grain production levels through altering the pricing for production quotas and thereby raising income levels of the rural residents. Statistics showed that when procurement prices went up during 1978-1984, poverty levels went down reduced, but when the prices were slashed later, poverty reduction stagnated.

Other Anti-Poverty Programmes

In addition to de-communisation and agricultural reform, the state also implemented several other programmes aimed at reducing poverty. There were three main anti-poverty programs – subsidised loans through the Agricultural Bank of China, the Food-for-Work programme through the he State Development Planning Commission, and the provision of development grants through the Ministry of Finance. The policies enjoyed varying degrees of success. As Donaldson points out, "overall, the most effective programs – such as the Food-for-Work program – appear to be those that work with the market, creating jobs and applying labour to building infrastructure that improves basic living standards (for instance, by improving access to water) and brings impoverished areas closer to markets".

Rightly so. In dealing with poverty, perhaps neither state nor market alone could alleviate the problems. As the paper concludes, "Understanding poverty reduction, in the specific case of China and also more generally, requires replacing a zero-sum approach to analysing state and market with a focus on the relationship between them".

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